Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation	)	MM Docket No. 93-215
	)	
and	)	
	)	
Adoption of a Uniform Accounting System for Provision of Regulated Cable Service	)	CS Docket No. 94-28

REPLY

U S WEST, Inc. ("U S WEST"), by its undersigned counsel, hereby submits this Reply to the Response of the United States Telephone Association ("USTA") to Petitions for Reconsideration ("USTA Response") of the Federal Communications Commission's ("Commission" or "FCC") Cable Cost-of-Service Order in the above-captioned dockets.[1]

I. REGULATORY PARITY BETWEEN THE CONVERGING CABLE AND TELEPHONE INDUSTRIES IS A LAUDABLE OBJECTIVE

U S WEST agrees with USTA that, in many respects, the cable

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[1] In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation and Adoption of a Uniform Accounting System for Provision of Regulated Cable Service, MM Docket No. 93-215, CS Docket No. 94-28, Report and Order and Further Notice of Proposed Rulemaking, FCC 94-39, rel. Mar. 30, 1994 ("Cable Cost-of-Service Order"). This Reply is filed pursuant to the comment schedule set forth in the public notice published in the Federal Register on June 1, 1994. 59 Fed. Reg. 28386. While other parties filed comments in response to the petitions for reconsideration filed, U S WEST is responding here only to the USTA Response.

and the local exchange telephone industries are converging.[2] Each will be facing significant technological change and increasing competitive risks in the years ahead; indeed, the likelihood is that cable companies and local exchange carriers ("LEC") will be using new fiber and broadband technologies to compete directly with each other before too much time has passed.[3] For that reason, U S WEST shares USTA's view that "the FCC's ultimate goal must be regulatory parity between telephone and cable . . . rules[,]"[4] so that regulation does not become the decisive factor in one industry prevailing over the other. For example, USTA, citing to Bell Atlantic's Opposition,[5] notes that the cable price cap or benchmarking plan[6] is "more favorable in crucial respects than the [price cap] rules for telephone companies."[7] USTA is quite correct in advocating that the Commission should "correct the inequities between the two regulatory frameworks by reforming the LEC price cap plan[;]"[8]

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[2]USTA Response at i.

[3]Id. at 2-4.

[4]Id. at 8.

[5]See In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, Opposition of Bell Atlantic to Petitions for Reconsideration, MM Docket Nos. 92-266 and 93-215, filed June 16, 1994 at 1.

[6]For a description of the Commission's benchmarking plan for cable rates, see In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, FCC 94-38, rel. Mar 30, 1994 at ¶ 1.

[7]USTA Response at 13.

[8]Id.

where "cable is subject to far fewer regulatory burdens"[9] than telephony, that imbalance should be righted, and regulatory parity achieved, by removing unnecessary regulatory burdens from local exchange telephone companies.

II. REGULATORY PARITY SHOULD MEAN INCREASING REGULATORY FLEXIBILITY FOR BOTH INDUSTRIES AS COMPETITION EVOLVES -- NOT SADDLING ONE INDUSTRY WITH THE ARCHAIC REGULATORY BURDENS OF THE OTHER

U S WEST disagrees with the particulars of USTA's advocacy, however, where the USTA position would result in increasing the regulatory burden placed upon the cable industry. USTA argues that the LECs' rate of return should not be deemed unreasonable for cable companies,[10] and that the treatment of cable intangible assets "should be identical to that afforded to goodwill acquired by LECs."[11] It is tempting to argue that, in effect, if LECs have to suffer with certain regulatory burdens, then the cable industry should have to do so as well. This is not, however, an appropriate or useful approach to regulatory parity. Placing outdated telecommunications regulation on the cable industry is not the answer, and would be a step backwards. Rather, regulation in both industries should be understood and structured as a transitional step until full competition is achieved, and should allow for sufficient flexibility both to

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[9] Id.

[10] USTA does acknowledge that cable companies will be able to "submit evidence . . . that a reasonable rate of return for the cable industry differs from the 11.25% that the FCC has prescribed for the interim." Id. at 7.

[11] Id. at 10.

stimulate and to accommodate that competition as it evolves.

III. THE RATE OF RETURN FOR ONE INDUSTRY IS NOT AUTOMATICALLY APPROPRIATE FOR ANOTHER

USTA argues that the 11.25 percent rate of return currently used by the Commission for the local exchange telephone industry should not be rejected out of hand for use in cable cost-of-service ratemaking because, contrary to the views expressed in the petitions for reconsideration, the relative levels of risk faced by the industries are comparable.[12]

U S WEST agrees that the "LECs face very significant risks which investors take into account in evaluating the attractiveness of telephone investments[,]"[13] and that the levels of regulatory and competitive risk currently faced by both industries is quite substantial. Nonetheless, risk alone is not the only factor to be considered in calculating the appropriate rate of return. The Commission's 11.25 percent rate of return figure for the LECs was developed after an in-depth review of the telecommunications industry. Although the cable and telephone industries are indeed converging, the capital structures of these industries are very different. For this reason alone, it is inappropriate, even on an interim basis, to impose an 11.25 percent rate of return on cable companies in cost-of-service proceedings, until such time as evidence of the capital structure of the cable industry can be properly developed and analyzed for that purpose. U S WEST does agree with USTA that the Commission

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[12] Id. at 7.

[13] Id.

should "reject any claims by the cable industry that a rate of return is unreasonable for them simply because it is the same figure that the FCC uses for the local exchange telephone industry."[14] The Commission also would have no basis, without further analysis, for saying that the 11.25 percent figure is reasonable for the cable industry simply because that is what its careful examination of LEC cost of capital happened to yield.

This does not mean that U S WEST rejects the application of principles of regulatory parity in this instance. On the contrary, U S WEST believes that the same methodologies should be applied in determining the appropriate cable rate of return as was used to determine the LEC rate of return. Parity does not require, however, that the identical rate of return figure itself be used for both industries.

IV. THE TREATMENT OF INTANGIBLE ASSETS ADVOCATED BY USTA IS INAPPROPRIATE FOR THE CABLE INDUSTRY

USTA proposes a "transition mechanism" for rate base treatment of intangible assets in the nature of goodwill: that those acquired prior to the passage of the Cable Act of 1992 be amortized over a fifteen year period, and those acquired after passage of the Act be excluded from the rate base in their entirety.[15] U S WEST agrees with the Commission that there is a "possibility that disallowance of any excess acquisition costs could have an adverse impact on the cable industry."[16] As such,

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[14] Id.

[15] Id. at 10-12.

[16] Cable Cost-of-Service Order, ¶ 50 n.178.

U S WEST cannot support any proposal that would so rigidly preclude cable operators from even making a showing that allowing such costs into the rate base would be in the public interest.

Intangible assets represent real, not phantom, costs to investors in the cable industry. Acquisitions in the cable industry have in the past been a primary means of bringing the capital needed to upgrade and improve cable networks so that they can remain competitive in the new multimedia environment. Any regime that restricts the recovery of such costs (even if only through a "backstop" mechanism that cable operators are not required to use for ratemaking purposes) could serve to inhibit cable acquisitions -- and thereby to staunch the flow of capital into the industry at a time when network upgrades and improvements are crucial to competitive strength.

Moreover, intangible assets are recognized costs of doing business under generally accepted accounting principles ("GAAP"). The Commission's general approach has been to follow GAAP where appropriate.[17] Here, following GAAP would allow the Commission to achieve its goal of placing the cable industry on a competitive footing (in terms of attracting capital, etc.), since these are the same cost rules applied to all competitive industries. Following the USTA Response, on the other hand, would deprive cable companies of a source of capital by providing

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[17] See, e.g., 47 CFR § 32.16; In the Matter of Revision of the Uniform System of Accounts for Telephone Companies to Accommodate Generally Accepted Accounting Principles (Parts 31, 33, 42, and 43 of the FCC's Rules), Report and Order, 102 FCC 2d 964 ¶ 2 (1985); In the Matter of Accounting and Ratemaking Treatment for the Allowance for Funds Used During Construction (AFUDC), Notice of Proposed Rulemaking, 8 FCC Rcd. 2084, 2086 ¶ 15 (1993) ("we prefer the use of GAAP in our accounting rules.").

a disincentive to investors to prefer cable investment over other investment vehicles.

V. CONCLUSION

If the cost-of-service ratemaking methodology is to be offered as an alternative to benchmarking, it should be a meaningful alternative. Its meaningfulness would be reduced, however, if the Commission were to impose a rate of return from another industry without any necessary relationship to cable's cost of capital, or to disallow from the rate base a genuine cost to the cable industry with a probable dampening effect on the industry's ability to attract investment. For these reasons, while U S WEST agrees with USTA that regulatory parity is important, U S WEST cannot support USTA's Response without reservation.

Respectfully submitted,

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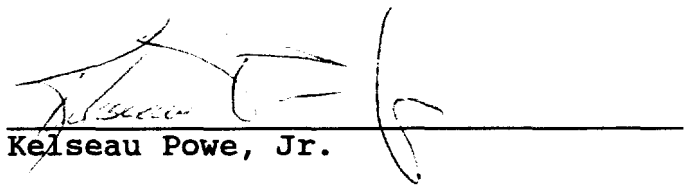
June 30, 1994

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify that on this 30th day of June, 1994, I have caused a copy of the foregoing **REPLY** to be served via first-class United States Mail, postage prepaid, upon the persons listed on the attached service list.



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